

of the noncontrolled section 902 corporation ending on or after April 20, 2009. See 26 CFR § 1.904-7T(f) (revised as of April 1, 2009) for rules applicable, except in the case of a taxpayer that makes the election under paragraph (f)(9) of that section, to dividends from a noncontrolled section 902 corporation that are paid in taxable years of the noncontrolled section 902 corporation beginning after December 31, 2002, and ending before April 20, 2009. See 26 CFR 1.904-7T(f) (revised as of April 1, 2009) for rules applicable, in the case of a taxpayer that makes the election under paragraph (f)(9) of that section, to dividends from a noncontrolled section 902 corporation that are paid in taxable years of the noncontrolled section 902 corporation beginning after December 31, 2004, and ending before April 20, 2009. However, taxpayers may choose to apply paragraph (f) of this section in its entirety in lieu of 26 CFR 1.904-7T(f) to all dividends paid in periods covered by the temporary regulations, provided that appropriate adjustments are made to eliminate duplicate benefits arising from application of paragraph (f) to taxable years that are not open for assessment.

(g) [Reserved] For further guidance, see § 1.904-7T(g).

[T.D. 8214, 53 FR 27034, July 18, 1988, as amended by T.D. 8412, 57 FR 20653, May 14, 1992; T.D. 9260, 71 FR 24533, Apr. 25, 2006; T.D. 9368, 72 FR 72590, Dec. 21, 2007; T.D. 9452, 74 FR 27881, June 11, 2009]

§ 1.904-7T Transition rules (temporary).

(a) through (f) [Reserved] For further guidance, see § 1.904-7(a) through (f).

(g) *Treatment of earnings and foreign taxes of a controlled foreign corporation or a noncontrolled section 902 corporation accumulated in taxable years beginning before January 1, 2007*—(1) *Definitions*—

(i) *Pre-2007 pools* means the pools in each separate category of post-1986 undistributed earnings (as defined in § 1.902-1(a)(9)) that were accumulated, and post-1986 foreign income taxes (as defined in § 1.902-1(a)(8)) paid, accrued, or deemed paid, in taxable years beginning before January 1, 2007.

(ii) *Pre-2007 separate categories* means the separate categories of income described in section 904(d) as applicable

to taxable years beginning before January 1, 2007, and any other separate category of income described in § 1.904-4(m).

(iii) *Post-2006 separate categories* means the separate categories of income described in section 904(d) as applicable to taxable years beginning after December 31, 2006, and any other separate category of income described in § 1.904-4(m).

(2) *Treatment of pre-2007 pools of a controlled foreign corporation or a noncontrolled section 902 corporation*. Any post-1986 undistributed earnings in a pre-2007 pool of a controlled foreign corporation or a noncontrolled section 902 corporation shall be treated in taxable years beginning after December 31, 2006, as if they were accumulated during a period in which the rules governing the determination of post-2006 separate categories applied. Post-1986 foreign income taxes paid, accrued, or deemed paid with respect to such earnings shall be treated as if they were paid, accrued, or deemed paid during a period in which the rules governing the determination of post-2006 separate categories (including the rules of section 904(d)(3)(E)) applied as well. Any such earnings and taxes in pre-2007 pools shall constitute the opening balance of the foreign corporation's post-1986 undistributed earnings and post-1986 foreign income taxes on the first day of the foreign corporation's first taxable year beginning after December 31, 2006, in accordance with the rules of paragraph (g)(3) of this section. Similar rules shall apply to characterize any deficits in the pre-2007 pools and previously-taxed earnings and profits described in section 959(c)(1) and (2) that are attributable to earnings in the pre-2007 pools.

(3) *Substantiation of post-2006 character of earnings and taxes in a pre-2007 pool*—

(i) *Reconstruction of earnings and taxes pools*. In order to substantiate the post-2006 characterization of post-1986 undistributed earnings (as well as deficits and previously-taxed earnings, if any) and post-1986 foreign income taxes in pre-2007 pools of a controlled foreign corporation or a noncontrolled section 902 corporation, the taxpayer shall make a reasonable, good-faith effort to reconstruct the pre-2007 pools of post-

1986 undistributed earnings (as well as deficits and previously-taxed earnings, if any) and post-1986 foreign income taxes following the rules governing the determination of post-2006 separate categories for each taxable year beginning before January 1, 2007, beginning with the first year in which post-1986 undistributed earnings were accumulated in the pre-2007 pool. Reconstruction shall be based on reasonably available books and records and other relevant information. To the extent any pre-2007 separate category includes earnings that would be allocated to more than one post-2006 separate category, the taxpayer must account for earnings distributed and taxes deemed paid in these years for such category as if they were distributed and deemed paid pro rata from the amounts that were added to that category during each taxable year beginning before January 1, 2007.

(ii) *Safe harbor method*—(A) *In general.* Subject to the rules of paragraph (g)(3)(iii) of this section, a taxpayer may allocate the post-1986 undistributed earnings and post-1986 foreign income taxes in pre-2007 pools of a controlled foreign corporation or a noncontrolled section 902 corporation (as well as deficits and previously-taxed earnings, if any) under one of the safe harbor methods described in paragraphs (g)(3)(ii)(B) and (g)(3)(ii)(C) of this section.

(B) *General safe harbor method*—(1) Any post-1986 undistributed earnings (as well as deficits and previously-taxed earnings, if any) and post-1986 foreign income taxes of a noncontrolled section 902 corporation or a controlled foreign corporation in a pre-2007 separate category for passive income, certain dividends from a DISC or former DISC, taxable income attributable to certain foreign trade income, or certain distributions from a FSC or former FSC shall be allocated to the post-2006 separate category for passive category income.

(2) Any post-1986 undistributed earnings (as well as deficits and previously-taxed earnings, if any) and post-1986 foreign income taxes of a noncontrolled section 902 corporation or a controlled foreign corporation in a pre-2007 separate category for financial

services income, shipping income or general limitation income shall be allocated to the post-2006 separate category for general category income.

(3) Except as provided in paragraph (g)(3)(ii)(B)(4) of this section, any post-1986 undistributed earnings (as well as deficits and previously-taxed earnings, if any) and post-1986 foreign income taxes of a noncontrolled section 902 corporation or a controlled foreign corporation in a pre-2007 separate category for high withholding tax interest shall be allocated to the post-2006 separate category for passive category income.

(4) If a controlled foreign corporation has positive post-1986 undistributed earnings and post-1986 foreign income taxes in a pre-2007 separate category for high withholding tax interest, such earnings and taxes shall be allocated to the post-2006 separate category for general category income if the earnings would qualify as income subject to high foreign taxes under section 954(b)(4) if the entire amount of post-1986 undistributed earnings were treated as a net item of income subject to the rules of § 1.954-1(d). If the high withholding tax interest earnings would not qualify as income subject to high foreign taxes under section 954(b)(4), then the earnings and taxes shall be allocated to the post-2006 separate category for passive category income.

(C) *Interest apportionment safe harbor.* A taxpayer may allocate the post-1986 undistributed earnings (as well as deficits and previously-taxed earnings, if any) and post-1986 foreign income taxes in pre-2007 pools of a controlled foreign corporation or a noncontrolled section 902 corporation following the principles of paragraph (f)(4)(ii) of this section.

(iii) *Consistency rule.* The election to apply a safe harbor method under paragraph (g)(3)(ii) of this section in lieu of the rules described in paragraph (g)(3)(i) of this section may be made on a separate category by separate category basis. However, if a taxpayer elects to apply a safe harbor to allocate pre-2007 pools of more than one pre-2007 separate category of a controlled foreign corporation or a noncontrolled section 902 corporation, such safe harbor (the general safe harbor described

in paragraph (g)(3)(ii)(B) of this section or the interest apportionment safe harbor described in paragraph (g)(3)(ii)(C) of this section) shall apply to allocate post-1986 undistributed earnings (as well as deficits and previously-taxed earnings, if any) and post-1986 foreign income taxes for the pre-2007 pools in each pre-2007 separate category of the foreign corporation for which the taxpayer elected to apply a safe harbor method in lieu of reconstructing the pre-2007 pools.

(4) *Treatment of pre-1987 accumulated profits.* Any pre-1987 accumulated profits (as defined in § 1.902-1(a)(10)) of a noncontrolled section 902 corporation or a controlled foreign corporation shall be treated in taxable years beginning after December 31, 2006, as if they had been accumulated during a period in which the rules governing the determination of post-2006 separate categories applied. Foreign income taxes paid, accrued, or deemed paid with respect to such earnings shall be treated as if they were paid, accrued, or deemed paid during a period in which the rules governing the determination of post-2006 separate categories applied as well. The taxpayer must substantiate the post-2006 characterization of the pre-1987 accumulated profits and pre-1987 foreign income taxes in accordance with the rules of paragraph (g)(3) of this section, including the safe harbor provisions. Similar rules shall apply to characterize any deficits or previously-taxed earnings and profits described in section 959(c)(1) and (2) that are attributable to pre-1987 accumulated profits.

(5) *Treatment of earnings and foreign taxes in pre-2007 pools of a lower-tier controlled foreign corporation or noncontrolled section 902 corporation.* The rules of paragraphs (g)(1) through (4) of this section apply to post-1986 undistributed earnings (as well as deficits and previously-taxed earnings, if any) and post-1986 foreign income taxes in pre-2007 pools, and pre-1987 accumulated profits and pre-1987 foreign income taxes, of a lower-tier controlled foreign corporation or noncontrolled section 902 corporation.

(6) *Effective/applicability date.* This paragraph (g) shall apply to taxable years of United States taxpayers begin-

ning after December 31, 2006 and ending on or after December 21, 2007, and to taxable years of a foreign corporation which end with or within taxable years of its domestic corporate shareholder beginning after December 31, 2006 and ending on or after December 21, 2007.

(7) *Expiration date.* The applicability of this paragraph (g) expires on December 20, 2010.

[T.D. 9260, 71 FR 24533, Apr. 25, 2006, as amended by T.D. 9368, 72 FR 72590, Dec. 21, 2007; 73 FR 15063, Mar. 21, 2008; T.D. 9452, 74 FR 27886, June 11, 2009]

§ 1.904(b)-0 Outline of regulation provisions.

This section lists the headings for §§ 1.904(b)-1 and 1.904(b)-2.

§ 1.904(b)-1 Special rules for capital gains and losses.

(a) Capital gains and losses included in taxable income from sources outside the United States.

(1) Limitation on capital gain from sources outside the United States when the taxpayer has net capital losses from sources within the United States.

(i) In general.

(ii) Allocation of reduction to separate categories or rate groups.

(A) In general.

(B) Taxpayer with capital gain rate differential.

(2) Exclusivity of rules; no reduction by reason of net capital loss from sources outside the United States in a different separate category.

(3) Capital losses from sources outside the United States in the same separate category.

(4) Examples.

(b) Capital gain rate differential.

(1) Application of adjustments only if capital gain rate differential exists.

(2) Determination of whether capital gain rate differential exists.

(3) Special rule for certain noncorporate taxpayers.

(c) Rate differential adjustment of capital gains.

(1) Rate differential adjustment of capital gains in foreign source taxable income.

(i) In general.

(ii) Special rule for taxpayers with a net long-term capital loss from sources within the United States.